

OFFICE OF TAX APPEALS
STATE OF CALIFORNIA

In the Matter of the Appeal of:

PATRICK LYNN ADDY
dba, COWGIRL CAFE

) OTA Case No. 19014248
) CDTFA Account No. 100-934999
) CDTFA Case ID 836625
)
)
)

OPINION

Representing the Parties:

For Appellant:

Patrick Lynn Addy, Taxpayer

For Respondent:

Kevin C. Hanks, Chief,
Headquarters Operations Bureau

For Office of Tax Appeals:

Richard A. Zellmer,
Business Taxes Specialist III

A. KWEE, Administrative Law Judge: Pursuant to California Revenue and Taxation Code (R&TC) section 6561, Patrick Lynn Addy, dba Cowgirl Cafe (appellant), appeals a decision issued by respondent California Department of Tax and Fee Administration (CDTFA) on appellant’s petition for redetermination of a July 3, 2014 Notice of Determination (NOD). The NOD is for \$171,622.40 in tax, plus accrued interest, and a negligence penalty of \$17,162.23, for the period October 1, 2009, through September 30, 2012 (audit period). Pursuant to the decision, CDTFA performed a reaudit and reduced the taxes from \$171,622.40 to \$104,398.00, and the penalty from \$17,162.23 to \$10,439.84, and otherwise denied the petition. This matter is being decided based on the written record because appellant waived the right to an oral hearing.

ISSUE

Whether appellant established a basis to reduce his sales tax liability.

FACTUAL FINDINGS

1. Appellant operates four western-themed breakfast diners in California, serving breakfast, sandwiches, and bakery items.
2. On January 10, 2012, prior to the start of the audit, CDTFA sent an auditor to observe one of appellant's restaurants.¹
3. By letter dated March 23, 2012, CDTFA notified appellant that his account was selected for an audit. During the audit, appellant explained to the auditor that he used cash register z-tapes² to prepare daily sales journals, which in turn were used to prepare his sales and use tax returns (SUTR's). Appellant provided daily sales journals but did not provide cash register z-tapes or a purchase journal for audit.
4. Appellant's taxable sales recorded in the daily sales journals exceeded reported taxable sales by \$44,580 for the audit period. Additionally, appellant's bank deposits from sales, excluding sales tax reimbursement, exceeded taxable sales reported on the SUTR's by \$409,391. Based on the discrepancies between appellant's records and appellant's reported taxable sales, CDTFA investigated further.
5. After auditing appellant's records, CDTFA determined that appellant's credit card sales ratio of 87 percent (as determined from a review of appellant's bank deposits) was higher than CDTFA expected, based on its experience with similar businesses. CDTFA observed the sales at each of appellant's four restaurants for two days. For each location, CDTFA divided sales paid for with credit cards by total sales for the two observation test days to compute an audited credit card sales ratio. The audited credit card sales ratios for the four locations were 50.34 percent, 53.13 percent, 74.54 percent, and 58.85 percent.
6. CDTFA used the credit card sales ratio method to compute appellant's audited taxable sales. For each location, CDTFA used the bank statements to compile credit card deposits for the audit period, and then divided the credit card deposits by the audited credit card sales ratio to compute audited taxable sales for each location.³ The audited

¹ Sales taxes were formerly administered by the Board of Equalization (board). Effective July 1, 2017, functions of the board relevant to this case were transferred to CDTFA. (Gov. Code, § 15570.22.) When referring to acts or events that occurred before July 1, 2017, CDTFA shall refer to its predecessor, the board.

² The z-tape is the part of the cash register tape that summarizes sales for certain periods of time.

³ CDTFA excluded sales tax reimbursement and tips from audited taxable sales.

taxable sales for all four locations combined totaled \$4,209,543 for the audit period.

Upon comparison to reported taxable sales of \$1,999,100, CDTFA computed unreported taxable sales of \$2,210,443 for the audit period.

7. On July 3, 2014, CDTFA issued the NOD to appellant for the underreported taxable sales, plus interest and penalties, which appellant timely petitioned.
8. On December 21, 2017, CDTFA issued a decision recommending a reaudit to expand the observation test to include one additional test day for each of the four locations.
9. Following the reaudit, CDTFA reduced the measure of underreported taxable sales to \$1,344,994.00. The adjustment reduces the tax liability to \$104,398.00, and the negligence penalty to \$10,439.84.
10. On January 19, 2019, appellant timely appealed CDTFA's decision on the basis that the auditor was never available to discuss the matter with him, the auditor did not perform a full reaudit and instead reduced the liability by 50 percent without discussing the matter with appellant, and appellant did not make this much money during 2009.⁴ Appellant provided no further explanation. Appellant also failed to provide any documentation or any other evidence to support these contentions.

DISCUSSION

California imposes sales tax on a retailer's gross receipts from the retail sale of tangible personal property in this state unless the sale is specifically exempt or excluded from taxation by statute. (R&TC, §§ 6012, 6051.) For the purpose of the proper administration of the Sales and Use Tax Law and to prevent the evasion of the sales tax, the law presumes that all gross receipts are subject to tax until the contrary is established. (R&TC, § 6091.) It is the retailer's responsibility to maintain complete and accurate records to support reported amounts and to make them available for examination. (R&TC, §§ 7053, 7054; Cal. Code Regs., tit. 18, § 1698(b)(1).)

When CDTFA is not satisfied with the amount of tax reported by the taxpayer, or in the case of a failure to file a return, CDTFA may determine the amount required to be paid on the basis of any information which is in its possession or may come into its possession. (R&TC, §§ 6481, 6511.) In the case of an appeal, CDTFA has a minimal, initial burden of showing that

⁴ On appeal, appellant did not dispute the negligence penalty and we do not discuss it further.

its determination was reasonable and rational. (See *Schuman Aviation Co. Ltd. v. U.S.* (D. Hawaii 2011) 816 F.Supp.2d 941, 950; *Todd v. McColgan* (1949) 89 Cal.App.2d 509, 514; *Appeal of Michael E. Myers* (2001-SBE-001) 2001 WL 37126924.) Once CDTFA has met its initial burden, the burden of proof shifts to the taxpayer to establish that a result differing from CDTFA's determination is warranted. (*Riley B's, Inc. v. State Bd. of Equalization* (1976) 61 Cal.App.3d 610, 616.) Unsupported assertions are not sufficient to satisfy a taxpayer's burden of proof. (See *ibid.*; see also *Appeal of Aaron and Eloise Magidow* (82-SBE-274) 1982 WL 11930.)

Here, CDTFA met its initial burden by establishing a discrepancy between appellant's records and appellant's reported taxable sales. Additionally, CDTFA established, by audit, that appellant's credit card sales ratio of 87 percent was higher than expected, which suggests that appellant did not report all of his cash sales. Aside from alleging that he lost money during "the great depression" of 2009, appellant failed to offer any other explanation for why his recorded taxable sales exceeded his reported taxable sales by \$44,580, or why his bank deposits from sales exceeded reported taxable sales by \$409,391. Appellant also failed to offer an explanation for the difference between his book credit card sales ratio of 87 percent, and the much lower credit card sales ratios observed by the auditor during the observation tests. We find these discrepancies to be unreasonable. Furthermore, appellant failed to provide any evidence or documentation to support that any adjustments are warranted to the audited liability. The burden is on appellant. (R&TC, § 6091.) Therefore, in absence of any supporting documentation or evidence, we have no legal basis to conclude that any adjustments are warranted.

HOLDING

Appellant failed to establish that any additional adjustments are allowable.

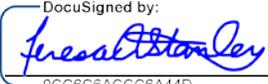
DISPOSITION

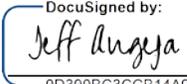
CDTFA’s action is sustained. The measure of unreported taxable sales shall be reduced from \$2,210,443 to \$1,344,994, as recommended by CDTFA. The appeal is otherwise denied.

DocuSigned by:

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Andrew J. Kwee
Administrative Law Judge

We concur:

DocuSigned by:

0CC6C6A0CC6A44D
Teresa A. Stanley
Administrative Law Judge

DocuSigned by:

0D390BC3CCB14A9
Jeffrey G. Angeja
Administrative Law Judge

Date Issued: 1/13/2020